Internal Control Evaluations

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Agenda

- Overview
- Components of the internal control framework
- OFM's department reviews, best practices, action plan
- Roles and responsibilities of management and internal audit staff
- Discussion of draft documents
- References

Overview

The State of Michigan follows the Committee on Sponsoring Organizations (COSO) framework.

From that guidance the State Budget Office, in consultation with the Auditor General, developed a "General Framework" to provide more details regarding internal control evaluations.

Components

Five Key Components:
- Control Environment
- Information and Communication
- Risk Assessment
- Control Activities
- Monitoring

Control Environment

- Attitudes and actions of management regarding controls
- The environment sets the organizational tone, influences control awareness, and provides a foundation for an effective control system.
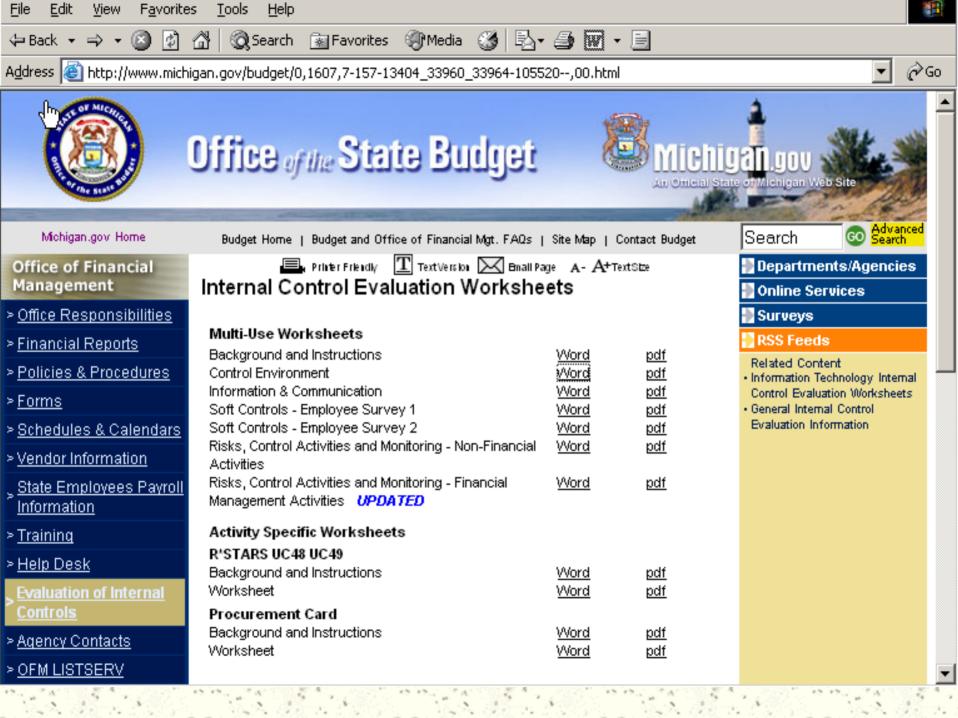
Control Environment

Factors include:

- Integrity and ethical values
- Commitment to competence
- Management philosophy and operating style
- Organizational structure
- Assignment of authority and responsibilities
- Human resource policies and practices

Control Environment

- Recommend that each department complete at least one assessment of these controls and additional evaluations if necessary for autonomous operating divisions.
- OFM's website includes an evaluation worksheet to assist in the evaluation of the control environment.

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Internal Control Evaluation Worksheets

Multi-Use Worksheets

Background and Instructions	Word	pdf
Control Environment	Word	pdf
Information & Communication	Word	pdf
Soft Controls - Employee Survey 1	Word	pdf
Soft Controls - Employee Survey 2	Word	pdf
Risks, Control Activities and Monitoring - Non-Financial Activities	Word	pdf
Risks, Control Activities and Monitoring - Financial Management Activities *UPDATED*	Word	pdf

Activity Specific Worksheets

R*STARS UC48 UC49

Background and Instructions	Word	pdf
Worksheet	Word	pdf

Procurement Card

Background and Instructions	Word	pdf
Worksheet	Word	pdf

Departments/Agencies

Online Services

Surveys

RSS Feeds

Related Content
• Information Technology Internal Control Evaluation Worksheets
• General Internal Control Evaluation Information

Information and Communication

- Each department must capture pertinent financial and non-financial information relating to internal and external activities.

- The information must be identified, captured, and communicated in a form and time frame that permits users to perform their duties effectively.

Information and Communication

Factors include:

- Relevant data
- Timeliness
- Communication up and down the organization
- Encouraging employees to offer suggestions
- And others
- OFM's website includes an evaluation worksheet to assist in the evaluation of the information and communication controls.

Risk Assessment

- Involves the importance of management identifying and evaluating factors that preclude it from achieving its mission.
- Risks relate to both department-wide and activity/program level objectives.
- Identifying and analyzing risks is a continuous process critical to maintaining effective internal control.

Risk Assessment

- A precondition to risk assessment is establishment of objectives, linked at different levels and internally consistent.

- Recommended approach is to use the risk assessment tool to identify entity level objectives and the activities, programs, initiatives, etc. which are critical to the department achieving its objectives. Then assess specific risks within those activities.

Control Activities

 - Control activities are the policies and procedures that help ensure management directives are carried out.
 - Control activities include a range of actions, such as approvals, authorizations, verifications, reconciliations, segregation of duties, and others.
 - Control activities help the department document the actions that will be done to minimize the identified risks.

Monitoring

- Involves assessing the quality of internal controls.
- Monitoring helps ensure that the control system is working as intended.
- Monitoring must be integrated into the everyday operations of the department.

Risks, Control Activities, & Monitoring Tools

- These three elements are combined on the evaluation worksheets.

- Financial management activities should be assessed by each department. A worksheet contains attributes for a variety of financial-related activities.

- Departments should use non-financial activities tool for the other high risk activities, programs, etc.

OFM Dept. Reviews, Best Practices, Action plan

- Reviewed each department's 2004 report and processes.
- Report available on OFM website
- Identified several best practices – use of websites, staff feedback, review programs, incorporating external audits.

OFM Dept. Reviews, Best Practices, Action plan

OFM developed a plan to:

- Encourage continuous monitoring.
- Improve the documentation supporting the reports.
- Improve IT evaluations.
- Align the Internal Auditors' role to be more in line with COSO.

Roles and Responsibilities

- Derived from COSO model and General Framework.
- Draft tools were created based on the application of these roles and responsibilities.

Roles and Responsibilities - Management

- Department Director - Act 431 of 1984 states that the department head of each principal department shall establish and maintain an internal accounting and administrative control system.

- COSO – "*Management is directly responsible for all activities of an entity, including its internal control system.*" "*The chief executive officer is ultimately responsible and should assume 'ownership' of the control system.*"

Roles and Responsibilities - Management

- ⌗ General Framework - Internal Control Officer (ICO) is responsible for coordinating the overall effort of evaluating, improving, and reporting on internal controls.

- ⌗ 50% of departments' internal auditors were the primary coordinators of the 2004 evaluation and reporting processes.

Roles and Responsibilities - Management

- Much of the departmental evaluation efforts should be assigned to dept. managers responsible for the various activities of the dept.

Roles and Responsibilities – Internal Auditors

- Evaluate the effectiveness of the control system.
- Independently verify the integrity of the department's control system.
- Provide technical assistance as requested by management.
- Offer conclusion whether the evaluation process has been conducted in accordance with the General Framework.

Creation of Draft Tools

- Inconsistency between written and oral assertions during dept. reviews.
- Workgroups to solicit feedback.
- Begin process of meeting with ICOs on a periodic basis to share initiatives, discuss control practices, provide guidance, etc.
- Internal Auditors expressed an interest in formulating conclusions and providing recommendations for improvement.

Draft Tools – Risk Assessment

- 11 criteria to assist in identifying activities/programs and IT applications that are critical to dept. achieving its overall mission and dept-wide goals and objectives.
- Instructions provided.
- Should subject all activities/programs to the risk assessment.

Draft Tools – Risk Assessment

- ICO should develop ranges for the overall scores, resulting in high, medium, and low risks.

- ICOs should modify the criteria or weighting factors as necessary to be relevant to the dept.

- At a minimum, high risk activities should be subjected to comprehensive evaluation and monitoring efforts.

Draft Tools – Risk Assessment

- Medium and low risk activities should have control systems documented with more extensive evaluation conducted as frequently as possible to have reasonable assurance regarding the controls for that activity.

- ICO should analyze the results of the risk assessment to ensure consistency in the criteria's application and consistency between the ICO and program staff regarding the activities' impact on the dept. wide mission.

- Questions or comments regarding the tool?

Internal Auditor Review Program

- Provides a step-by-step program to guide the Internal Auditor's review of the department's processes.
- Worked with Internal Auditors to identify key attributes of a sound system.
- Intended to result in consistency across departments, provide support for certifications.
- Questions regarding the review program?

ICO Certification Letter to Director

- Purpose is to identify attributes of a sound internal control evaluation and reporting processes.
- Allows the ICO to provide an assessment of the department's processes.
- Provides summary information that can be further reviewed by the Internal Auditor.

ICO Certification Letter to Director

- Tailored after representation letter for financial audits.
- The letter will also include an action plan for attributes not currently included in the department's processes.
- Questions regarding the letter?

Internal Auditor Certification Letter

- Attributes are consistent with items in the review program.
- Provides a means to agree or disagree with specific attributes, rather than a summary statement only.
- Improves the overall process by separating the lines of responsibility between the ICO and Internal Auditor.
- Questions?

Budgetary Controls

- Created a separate tool by extracting from the existing Financial Activities tool and added several questions.
- If agencies have distributed the "old" tool, manually add the questions. Otherwise new tool with highlights added to OFM website.
- Please use new tool in the future.

Material Weaknesses

- Please notify OFM (ringlerd1@michigan.gov) of any material weaknesses that departments intend to include in their final reports.

References

- OFM website – www.michigan.gov/ofm
  - General internal control evaluation information
  - Internal control evaluation worksheets
  - IT internal control evaluation worksheets
- General Framework
- COBIT (Control Objectives for Information and Related Technology)

Other questions or comments?